forces will ensure that ILECs' rate structures reflect how costs are incurred. At this stage, any inefficiencies that the ILECs could potentially create in their pricing structures will be eliminated because competitors will quickly respond by offering more efficient rate structures. In the face of competition, the ILEC will not be able to extract extraordinary profits from inefficient rate structures.

Elimination of Price Cap X-Factor. As Ameritech noted above, in Phase 1, the no-sharing X-factor for price cap carriers should be moved from its current 5.3% to the baseline 4%. This would eliminate the distorting effect that sharing has on LEC prices. Similarly, in Phase 2, the additional price distortions caused by any X-factor should be removed as well. The X-factor was established under price caps as a mechanism to force LECs to flow through assumed efficiency gains. In a competitive environment, it is competition itself that serves that function as prices tend to be driven toward incremental cost. Leaving the X-factor in place may well result in ILEC pricing that has little to do with underlying costs. Again, if prices are kept artificially low, competitive entry and investment is discouraged. Therefore, the Commission should eliminate the X-factor entirely from the price cap formula, no later than the time Phase 2 status is achieved.

V. A PRESCRIPTIVE APPROACH TO ACCESS REFORM HAS NO PLACE IN THE CURRENT TELECOMMUNICATIONS ENVIRONMENT.

As noted by Dr. Gordon, a prescriptive approach has no place in the pro-competitive deregulatory environment required by the Act.[84] At a time when entry barriers are virtually nonexistent, reversion to the old prescriptive paradigm will introduce distortions that will skew competitive entry and deprive customers of the benefit of competition on truly economic terms. Thus a market-based approach is clearly the correct method for managing the transition of ILEC access rates to competitive levels.

On the other hand, the prescriptive method is far less flexible and runs the risk of not being valid over the long run. The reason for this is that the prescriptive method requires assumptions about the future timing and intensity of competition that will likely not comport with reality. For example, if a prescriptive method were to move current access rates toward cost over a five year period the normal operation of the competitive marketplace could be stifled if significant market forces were to emerge during those five years.

In fact, prescription of rates in a competitive marketplace would have an anticompetitive effect. To the extent ILEC access rates are prescribed at levels that are below what would have been normal market levels, those rates will discourage entry or expansion by efficient competitors. If the ILEC access rates

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[84] Gordon Paper at 22-23.

are set above what would have been normal competitive levels, they will act as a price umbrella and will impair normal competition from CLECs. Unreasonably high ILEC access rates will also encourage entry by inefficient competitors whose costs are higher than the ILEC's but lower than its inflated rates.

Nor is prescription necessary to avoid a "price squeeze" as some IXCs claim.[85] As Dr. Gordon points out,[86] the conditions under which such a scheme could successfully be carried out are so remote as to make such conjecture whimsical.

Over the past four years, the Clinton administration has sought policies to create an economic climate conducive to physical capital investment.[87] The market-based approach is consistent with the administration's goal since the ILECs, whose annual investment in the network is over three times that of the combined investment of all IXCs and cable companies, will have an opportunity for a fair return on their investment. If the Commission decides to implement a prescriptive approach, the ILECs will not invest in the local network since it will not yield a fair return, thus retarding investment in the network contrary to the administration's goal.

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[85] NPRM at ¶ 47.

[86] Gordon Paper at 26-28.

[87] Economic Report of the President - Transmitted to the Congress, February, 1996 at 31.

In sum, use of a prescriptive method is a step back into the regulatory past -- where rates are set based upon a rate of return type considerations and entry was subject to regulatory control rather than market forces. As such, it is clearly inconsistent, not only with the Commission's price cap regime, but with the deregulatory and pro-competitive goals of the Act. It would indeed be ironic if the Commission sought to implement access reform under the Act through a rate prescription proceeding.

VI. TRANSITION ISSUES.

A. The Carrier Common Line Charge Should Reflect the Full Elimination of Long-Term Support.

Ameritech agrees with the Joint Board's recommendation that long-term support ("LTS") should not continue to be recovered through the CCL charge but that support to high cost LECs be provided instead through the new universal service mechanism.[88] However, Ameritech reiterates its strong objection to the Joint Board's suggestion that the residential and single-line business SLC cap be reduced by half the amount of the LTS (which would be eliminated in its current form). As Ameritech explained in its comments and reply comments on the Joint Board's Recommended Decision, that proposal would merely increase the implicit subsidy provided by long distance services to the recovery of loop costs caused by the provision of local exchange service. Instead, the CCL charge should be

[88] NPRM at ¶ 243.

reduced by the total amount of LTS recovery moved to the universal service support mechanism.

B. The Commission's Depreciation Rate Prescriptions Are Problematic.

Separately, the Commission asks whether its prescription of depreciation rates for use by the ILECs in the past have been at the appropriate level, or if an under-depreciation problem exists for the ILECs.[89] Ameritech has consistently maintained that the Commission's depreciation prescriptions have not reflected the economic realities of the changing marketplace and the technology demands of customers. As a consequence of these inadequate prescriptions, a significant depreciation reserve shortfall exists on the regulated books of account (the MR books). This reserve deficiency exists today and will be exacerbated in the future unless the ILECs are allowed to set depreciation rates at the appropriate economic levels. It makes no sense in a competitive marketplace to force the ILECs to retain grossly unreasonable rates of depreciation, especially when compared to the depreciation rates adopted by the ILEC competitors.

VII. THE REGULATION OF TERMINATING ACCESS FOR ALL LECs SHOULD BE THE SAME.

Ameritech concedes that a provider's ability to control prices is somewhat greater for terminating access than originating access.[90] For terminating access,

[89] Id. at ¶¶ 250-255, 266-270.

[90] Id. at ¶ 271.

the choice of access service provider is usually made by the called party in selecting a LEC. The decision to place the call and payment for the call lies, however, with the calling party. Neither the calling party nor the long distance service provider has much ability to influence the called party's choice of service provider. However, the "power" for terminating access is the same for all terminating access providers regardless of whether the provider is "dominant" or "non-dominant," incumbent or a new entrant. Therefore, Consistent regulatory safeguards should be placed on all providers of terminating access.

Ameritech's proposed regulations for terminating access are:

(1) Price cap LECs should continue to be subject to price cap regulation for terminating access under the terms of the Commission's market-based approach until a demonstration of substantial competition by the ILEC results in the Commission granting non-dominant status for the originating access service.

(2) For all non-dominant LECs (including those price cap LECs who have attained non-dominant status for originating access), the terminating access rate levels should be less than or equal to the lesser of their own originating access rate levels or the terminating access rate levels of the dominant LEC in the area (if there is one). In order to charge any higher rate, the non-dominant LEC would be required to provide cost support.

These minimal restrictions should be sufficient to guard against any inappropriate exercise of power. This is especially true in light of the fact that any power is not unlimited. For medium and large businesses, many IXCs bypass terminating switched access charges by utilizing dedicated facilitates. These arrangements are commonly called terminating switched access arrangements and have already become part of the buying criteria of medium and large business customers. IXCs or competing LECs facing excess terminating access rate levels by either a dominant or non-dominant LEC will have an incentive to win the end user customer and reap the savings by avoiding the excessive terminating access rates. Excessive terminating access rates may also be self-policed within the industry since both dominant and non-dominant LECs will be charging each other for terminating access and will attempt to avoid being charged excessive rates.

The Commission should not require ILECs to price terminating access service at forward-looking economic costs. The switch capacity investments made by ILECs over past years have been with the express intent to serve the needs of the IXC marketplace. During this time period, the Commission has controlled the depreciation rates and price levels by which these switch investments have been allowed to earn a financial return. Historically, the Commission has deliberately set depreciation lives longer than the economic lives of equipment would have warranted. To change the method of pricing terminating access to forward-looking costs now would ignore the past investments made to serve the access market place. Requiring terminating access be priced at forward-looking costs places the cost of switches installed in the 1980's and early 1990's on the ILECs' shareholders instead of the users of these switches. This would amount to confiscation.

The Commission suggests that one alternative for regulating provision of terminating access is to adopt a called-party-pays methodology akin to that used by wireless companies for access charges for air time.[91] From a practical approach because of the potential for customer confusion, regarding who pays for what and what the rate is to the end user, this mechanism should not be mandated.

Another proposed approach involves charging nothing for terminating access and charging, in essence, double for originating access. This option is severely flawed and must not be required by the Commission. It is uneconomical to recoup the costs of both originating and terminating access in the originating access rate. Loading terminating costs into originating minutes creates an uneconomic incentive to bypass originating switched access. Small business and residential customers that are unable to bypass originating access as easily as medium and large business customers would pay a disproportionately large share of public switched network costs and subsidize big businesses' terminating traffic on the network.

VIII. PART 69 ISSUES.

A. Equal Access Network Reconfiguration Costs.

The Commission asks whether it should require incumbent price cap carriers to make exogenous cost decreases to one or more of the PCIs to account for the completion of the amortization of equal access network reconfiguration

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[91] Id. at ¶ 275.

("EANR") costs on December 31, 1993.[92] Ameritech began booking EANR in approximately October, 1985, and completed the amortization on December 31, 1993. Subsequently, the Commission considered whether to apply an exogenous cost adjustment as part of its review of the 1994 annual access filing and later in the context of the LEC price cap performance review.[93] In neither case did the Commission find reason to require an exogenous adjustment, nor is there any reason to do so now.

This issue has already been litigated and there is no reason to reopen it here. Further, implementing an exogenous change for these costs would undercut the Commission's goal that rates under price caps be driven by competition and market economies.[94] Moreover, the change would also require that other cost issues be opened for exogenous treatment, especially those that might justify an index increase. Finally, under the Commission's new standard for exogenous cost treatment (i.e., only "economic" cost changes merit exogenous treatment),[95] the end of this cost amortization would clearly not qualify.

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[92] Id. at ¶ 293.

[93] LEC PriceCap Performance Review Order at ¶ 305.

[94] Id. at ¶ 294.

[95] Id. at ¶ 293.

B. Part 69 Allocation Rules.

Subparts D and E of Part 69, allocate investment and expenses to all the access rate elements. Regardless of whether the Commission adopts a market-based or a prescriptive approach to access reform, the need for allocating costs to these access rate elements is no longer needed.[96] The rules which require fully distributed costs to be spread across the different rate elements are no longer needed for price cap carriers. The elimination of the requirement for price cap carriers to utilize Subparts D and E should be immediate. The impact to price cap carriers would be transparent.

C. Part 69 Waivers.

The Commission has noted that, over the years, several LECs have established access rate elements or subelements pursuant to waiver.[97] It asks whether these waivers should be incorporated into Part 69. As noted above, Part 69 should be changed to permit LECs the flexibility to introduce new switched access rate elements. However, to the extent such relief is delayed it makes sense to permit all carriers to have the advantage of waivers previously granted. This will enable the introduction of new elements quickly without needless petitions and filings -- providing a benefit to those carriers' customers.

[96] NPRM at ¶ 294.

[97] Id. at ¶ 299.

IX. CONCLUSION.

The Commission is headed down the right track with its proposed rate structure modifications and market-based approach for reforming access charges. Anything less than letting the market work would be inconsistent with the pro-competitive deregulatory mandates of the Act and the Commission's own goal to promote a fully competitive marketplace. A "prescriptive" approach to reforming access would ignore the already significant changes taking place in the access market in response to competitive pressure -- ILEC reductions and attempts to introduce new services and pricing plans.

The plan the Commission ultimately adopts should remove and make explicit subsidies currently embedded in access charges, realign the access rate structure to more closely reflect cost causation, and provide significant relief from pricing restrictions and price cap regulation as the stage for local competition is set and actual competition access and local fully develops.

The competitive environment is developing quickly. It is important that the Commission keep in mind its pro-competitive, deregulatory goals and, in this proceeding, carefully modify access regulations to remove existing economic inefficiencies and distortions and not inadvertently create new ones.

Respectfully submitted,

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Dated: January 29, 1997

ATTACHMENT A

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Ameritech

Anthony M. Alessi
Director
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December 6, 1996

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, NW
Room 222
Washington, DC 20554

RECEIVED
DEC 6 '96
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

Re: **Ex Parte Statement**
Access Reform

Dear Mr. Caton:

The attached letter addressed to Ms. Regina Keeney, Chief, Common Carrier Bureau from Mr. Gary Lytle, Vice President - Federal Relations should be incorporated in the record of the forthcoming Notice of Proposed Rulemaking on Access Reform at the time the docket is initiated. The letter was provided to Ms. Keeney by Mr. Lytle at a meeting on access reform that occurred on December 5, 1996.

Sincerely,

Anthony M Alessi

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Ameritech.

Gary R. Lytle
Vice President
Federal Relations

December 5, 1996

Ms. Regina Keeney
Chief, Common Carrier Bureau
Federal Communications Commission
1919 M Street, NW
Room 500
Washington, DC 20554

Dear Ms. Keeney:

In recent months, Chairman Hundt and the other Commissioners have spoken about the importance of access reform and the Commission's intent to address it. Ameritech, too, strongly believes that access reform is essential and has given serious consideration to developing a proposal that can meet critical public policy objectives, such as promoting a competitive marketplace and maintaining affordable and reasonable rates for telecommunications services. Ameritech requests that the attached Ameritech proposal be given full consideration in the forthcoming notice of proposed rulemaking on access reform.

Although Ameritech expects to elaborate fully on the need for access reform when the Commission issues its notice, Ameritech would like to note at this time that current pricing restrictions and subsidy mechanisms were predicated on an environment devoid of access competition -- one that, especially in light of the Telecommunications Act of 1996, no longer exists. Thus, access reform must, at a minimum, result in acceptable and competitively neutral ways for all incumbent LECs to continue any public policy subsidies that are determined to be necessary and appropriate. In addition, reform must address restrictions on LEC pricing of access and interexchange services that are unnecessary and counter-productive in a competitive environment.

Failure to achieve either (or both) of these ends could result in a significant disincentive for the incumbent LECs to continue to invest in the nation's telecommunications infrastructure and maintain low basic exchange rates in their role as the current providers of universal service. The ILECs today invest approximately 20 billion dollars annually in maintaining and improving the telecommunications "infrastructure" -- three to four times as much as interexchange carriers and cable companies combined. Impairing ILEC's ability to recoup their costs and to provide a reasonable return to their investors would create a natural incentive for the incumbents to invest their money elsewhere.

Ameritech believes that its access reform proposal is a balanced approach that can be utilized by the industry as a whole, and will bring needed certainty to the marketplace. Additionally, it has the advantage of being adaptable so as to accommodate decisions that are made by the Commission with respect to interconnection, universal service, and other related matters. Finally, it is not a make-whole proposal. There is full recognition by Ameritech that the dynamics of the marketplace will greatly affect access charge levels as 1+ intraLATA presubscription and unbundled network elements are introduced. Furthermore, it contemplates a transition towards the elimination of the transport interconnection charge (TIC). At the same time, it calls for substantial changes to price caps and proposes pricing flexibilities that would enable the industry to move forward into a new competitive marketplace.

The competitive environment is changing drastically and with great speed. As the Commission well knows, it is important that its regulations be modified in response to those changes so as not to create any inappropriate distortions. Ameritech submits that the attached proposal would achieve that result.

Sincerely,

Gary R. Lytle

Attachment

AMERITECH ACCESS REFORM PROPOSAL

I. Introduction

Dramatic and rapid changes in the telecommunications market accelerated by the Telecommunications Act of 1996 (the Act), coupled with historical distortions in the current access charge structure create an urgent need for the Federal Communications Commission to reform access charges. Current prices for access are burdened by implicit subsidies, based on the now-archaic assumption that rates did not have to reflect the costs of providing service. In today's quickly evolving environment, these implicit subsidies and pricing restrictions are no longer a viable means of achieving the public policy goal of maintaining affordable local service rates. Access reform and the universal service review now underway are inextricably linked and must be dealt with together to ensure the preservation and proper collection of the subsidies that are necessary to maintain, affordable basic exchange rates. Access reform and universal service must not discourage investment in the nation's telecommunications infrastructure. And finally, access reform and universal service must permit customers to realize the benefits of competition, in pricing and services.

Ameritech's Access Reform proposal builds upon the proposal which Ameritech submitted to the Commission in the Universal Service proceeding (Dkt. 96-45). Recognizing the desire of regulators to avoid significant rate increase for consumers, to continue the historical recovery of interstate loop and line port cost recovery directly from interstate providers of telecommunications services and not disturb rates paid by consumers. The access reform proposal presented in this paper provides additional detail on how to implement Ameritech's original proposal through access reform and provides a framework for additional access pricing flexibility.

The starting point for our proposal is the recognition that the Act expressly continues policies that have been in place over the past 60 years to create and distribute subsidies to rural, residential and other designated customers. The Act does not eliminate these policies but continues them with specific mandates. Specifically, the Act requires that:

- basic services should be made available at affordable rates, without the reference to the cost of providing such services (Section 254 (b)(1));

- in general, rates for all telecommunications services, including advanced services, should be comparable between rural and urban areas (Section 254 (b)(3));

- specifically, interexchange providers must charge rates in rural and high cost areas that are no higher than rates charged in urban areas (Section 254 (g));

- there must be specific, predictable and sufficient federal and state mechanisms to preserve and advance universal service (Section 254 (b)(5)); and

- every telecommunications carrier that provides interstate telecommunications services shall contribute, on an equitable and nondiscriminatory basis, to the specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service (Section 254 (d)).

Congress did not direct that subsidies be eliminated, but that they be removed from rates where they implicitly exist today, made explicit and collected on a competitively neutral basis. Just as the Joint Board has reviewed the subsidies required to support high-cost areas and low-income subscribers, so too must the Commission deal with the implicit subsidies built into access charges to support affordable consumer rates. The calls of long distance carriers to immediately bring their access charges down to cost and eliminate the support those carriers currently provide to maintain affordable basic exchange rates is directly in conflict with this congressional mandate.

Fundamentally, as stated in Ameritech's universal service proposal, a straight forward option for maintaining end user rates where they are would be for the Commission to continue the historical recovery of at least 25% of basic exchange service (loop and line port) costs from interstate providers of telecommunications service. But, in so doing, the Commission must develop a collection mechanism which is competitively neutral and does not distort the natural workings of a competitive market place. Ameritech's access reform proposal comprehensively addresses these needs and by recommending the following:

1) Subsidies should be removed from switched access rates and collected in a competitively neutral manner.

2) Switched access rate elements are realigned to recover non-traffic sensitive costs on a flat rated basis, and usage sensitive costs on a usage rated basis.

3) Identifiable costs are removed from the Transport Interconnection Charge (TIC) and moved to the proper rate elements.

4) Price cap regulation is simplified.

5) Access pricing is made more flexible for the competitive market.

The remainder of this paper provides the details and justification for Ameritech's Access Reform proposal.

II. Switched Access Rates Today Are Distorted By Subsidies.

Today, access rates are burdened by subsidies in two ways. First, subsidies result from collecting the costs specifically associated with the provision of one service, such as basic exchange, in the pricing of another service, such as interstate access[1]. Second, subsidies arise generally when access revenues have contributed to fill the gap between basic exchange revenues and the costs of providing basic local exchange service.

[1]Similarly, subsidies are created when the costs of small LECs are collected from the rates a different LEC charges for access.

Within switched access, the Carrier Common Line ("CCL") charge, the Information Surcharge, the Local Switching charge and the TIC all have identifiable subsidy components. Ameritech's proposal identifies those components and proposes a mechanism to remove them from access rates while continuing to recover the costs from interstate telecommunications providers. Sections A and B, of this proposal, will first identify the subsidies embedded in each switched access rate element and then propose new mechanisms to collect these subsidies.

A. Access Subsidies

Carrier Common Line charge

The most critical subsidy vehicle for reform is the CCL charge. The sole purpose of the CCL is to serve as a vehicle to collect subsidies from interstate toll services to keep basic exchange rates affordable. However, the CCL charge does not operate in a competitively neutral manner since it is assessed as a surcharge on the ILECs' switched access -- a service to which it bears no cost relationship whatsoever, The CCL is exactly the type of implicit subsidy that must be reformed under section 254 of the Act.

Today, the CCL charge is comprised of four components, each of which is a subsidy. The first component is NECA long-term support ("LTS") that subsidizes high-cost carriers' interstate loop cost recovery. These costs are not directly related to the cost structure of the LEC collecting the subsidy. Nonetheless, the LTS increases the price of the ILECs' local switching services, amounting to an incentive for interexchange carriers ("IXCs") to seek alternative access sources[2]. For Ameritech alone, the LTS is approximately $60 million per year.

The second component of the CCL charge is the base factor portion overflow ("BFPO"). The BFPO is directly related to loop costs that are assigned to the interstate jurisdiction but

[2]The Commission has already tentatively concluded that including LTS cost recovery in the CCL charge is inconsistent with the requirements of the Telecommunications Act of 1996. See, CC Docket 96-45 Notice of Proposed Rulemaking @ 113

not recovered from end users via the Interstate End User Common Line ("EUCL") charge. This is assessed to purchasers of ILEC switched access services and directly subsidizes basic local exchange rates (primarily residential and single-line business subscribers). Ameritech collects $165 million each year from the BFPO.

The third component of the CCL is the recovery of payphone service costs allocated to the interstate jurisdiction. Ameritech recently removed these costs from the CCL charge and implemented a separate "set use fee" assessable on interstate calls originating from its payphones. This action has recently been ratified by the Commission in CC Docket 96-128, in which the Commission directed all LECs to remove the interstate costs of their payphone sets from the CCL charge. A separate compensation mechanism will be implemented to recover these costs.

The last component of the CCL charge recovers the costs associated with the ILECs' inside wire amortization. The Commission determined that these costs should be recovered through the CCL so as not to burden end users who benefit from and use this wire[3]. Conceptually, these are identical to the loop costs included in the BFPO.

<u>The Information Surcharge</u>

The Information Surcharge is also assessed to purchasers of switched access on a per minute of use ("MOU) basis, and is a subsidy paid from interstate access service. It recovers the costs of white pages directory production. These costs, however, are caused by the provision of exchange service to the end user subscriber, not as a result of the provision of switched access. Ameritech receives $10 million annually from the Information Surcharge.

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[3]In the case of Ameritech, a small amount of inside wire cost recovery still remains in the CCL charge - approximately $10 million associated with the decision of Illinois Bell to establish demarcation points in multi-tenant and multi-story buildings at the minimum point of entry. The decision was implemented several years before the Commission's decision in CC Docket No. 88-57.

Local Switching Charge

The current local switching charge, to the extent that it recovers nontraffic sensitive costs associated with the line port in the switch and main distribution frame, also subsidizes basic exchange service. These costs are incurred with the provision of an individual local loop. Thus, as with other loop related costs, recovery of non-traffic sensitive line port costs from local switching constitutes a subsidy. In Ameritech's case, this is a $110 million interstate subsidy to basic exchange service paid by purchasers of switched access service.

The Transport Interconnection Charge ("TIC")

The TIC is assessed on all purchasers of access local switching service - including those that utilize direct-trunked or CAP provided transport. The TIC recovers costs associated with tandem switching and termination, and SS7 related services and as such, acts as a subsidy to those services.

Above and beyond the historical 25/75 allocation of basic service costs between the federal and state jurisdictions, access rates have more generally supported basic local exchange rates, which as a whole do not recover the 75% of loop and port costs remaining in the intrastate jurisdiction. As presented in Ameritech's Universal Service proposal, today, the Ameritech-wide loop and line port costs total $4.3 billion on an embedded cost basis. Yet, Ameritech recovers only $3.1 billion of that directly from end users in the form of intrastate local exchange rates and the EUCL. As discussed above, the BFPO and inside wire amoritization portions of the CCL recover an additional $175 million, the line port portion of the Local Switching Charge recovers $110 million and the Information Surcharge provides $10 million. Nonetheless, there is still a shortfall of $905 million between revenues and costs. Without other specific collection mechanisms, the ability of the LEC to keep basic local exchange service rates at current levels is predicated on maintaining margins above costs on other services, including access[4].

[4]With the enactment of the Telecommunications Act of 1996 and the Commission's Interconnection Order, today's sources of contribution to the maintenance of low basic exchange rates cannot be sustained. New

B. The Access Subsidy Solution

As required by the Act, Ameritech's proposes to continue interstate subsidies in an explicit, competitively neutral manner. The recommended solution can be implemented by all LECs. As discussed, the foundation of this proposal is that at least 25% of the cost of the loop and line port[5] be recovered in the interstate jurisdiction in order to insure that end users continue to enjoy affordable basic exchange service rates.

1. 25% of Loop and Line Port Cost Recovery

A key element of Ameritech's access reform proposal is the creation of a mechanism to recover the portion of the local loop and line port costs allocated to the interstate jurisdiction. This mechanism consists of the existing EUCL charged directly to the end users, and a charge that will recover the difference between a total of 25% of the loop and line port costs and the EUCL revenues. This charge will be assessed on interstate communications providers - the carriers which provide the retail services that currently subsidize local exchange services. For purposes of this proposal, this charge will be called the Loop/Port Recovery ("LPR") charge. To further the interests of universal service and to be consistent with Section 254(d) of the Act, the LPR charge should be assessed to interstate telecommunications providers in a competitively neutral fashion in a way that does not skew their access purchase decision.

The Commission has a number of options regarding how to collect the LPR on a competitively neutral basis. First, it can assess the LPR charge as specifically contemplated by Section 254 (d), on all providers of interstate telecommunications services. In this case, a single third-party entity could aggregate the appropriate costs from all eligible LECs and bill each interstate provider on the basis of total interstate retail revenues. A second possibility would be to implement a similar mechanism on a LEC/study area (state) specific

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market entrants will provide service through the use of their own facilities or the incumbent's unbundled network elements, which will be priced at cost through the TELRIC methodology.

[5] The interstate allocation of loop costs is currently 25%. The interstate portion of the loop port varies by study area, but 25% would be a reasonable surrogate if a common allocation is desired for all LECs.

basis with billing done on the basis of relative interstate retail revenues within the state or study area.

With the implementation of the LPR charge, the BFPO and inside wire portions of the CCL and the Information Surcharge would be eliminated and the line port costs would be removed from the Local Switching rate element.

2. Long Term Support

As recommended by the Joint Board, the LTS should be removed from the CCL charge in the Commission's universal service inquiry. If LTS is treated otherwise in the Commission's final decision, then it should be directly billed by NECA to the IXCs. There is no reason to continue to burden LEC switched access services with this surcharge, and indeed the Act does not allow it. Since LTS is a subsidy which is ultimately paid by the IXCs today, there is no reason not to eliminate the intermediate step and to reconfigure the subsidy flow as a direct billing by NECA to IXCs.

C. Switched Access Rate Realignment

Within today's switched access rates, there are some costs which are recovered via inappropriate rate elements or on an inappropriate recovery basis. The following discussion proposes modifications to the Local Switching Rate Element, and the TIC to eliminate these concerns.

1. Local Switching

With line port cost recovery removed from local switching and placed in the LPR charge, the remainder of the local switching charge should be designed to recover costs in a manner consistent with how they are incurred. A flat-rated monthly Trunk Port charge to recover the non-traffic sensitive cost of the trunk port should be established. The remainder of the traffic sensitive costs of local switching should continue to be recovered by the Local Switching charge on a MOU basis.

2. TIC

As discussed in Section II, A, the TIC recovers costs associated with tandem switching and termination as well as SS7 related costs. Theses costs should be moved to existing rate elements that are assessed to the users of tandem and SS7 services. Ameritech has already established separate rate elements for SS7 signal generation, switching, and transport and has reduced the Ameritech TIC rate by a corresponding amount.

Because of the significance of the TIC in contributing to the LECs' ability to maintain affordable basic exchange rates, the Commission should permit the remainder of the TIC to be billed to interstate providers of telecommunications services in a manner consistent with the way in which the LPR is billed. These amounts should no longer be embedded in switched access rates and instead, should be recovered on a competitively neutral basis from all providers of interstate services. The Commission should reject the interstate carrier's demands for an immediate flash-cut elimination of the TIC since that could jeopardize the LECs' ability to provide affordable basic local exchange services. However, a phase out of the TIC in equal increments over five years might be appropriate with reform of current access pricing restrictions (see sections D and E, following). Such reforms must give the ILECs the flexibility to adjust rates, including rate increases where justified by the value of services. In addition, since we have demonstrated that the TIC in its entirety does not cover the deficit between the cost of providing basic exchange service and the revenue collected for that service, the TIC should not be eliminated until states have completed studies of intrastate subsidy sources that contribute to affordable basic local exchange rates. In a competitive environment, and where ILECs are required to provide unbundled elements at TELRIC based rates, LECs can no longer count on margins from other services (e.g., vertical service and toll) to maintain low basic local exchange rates, and have instituted competitively neutral mechanisms for identifying and collecting these subsidies. States must begin and conclude proceedings that allow LECs to recover the intrastate portion (75%) of loop and line port costs from end user rates or state universal service funding mechanisms currently being recovered by the TIC.